

House Regulatory Reform Committee
December 7, 2016
Senate Bill 448 (H-2) Draft 5

Statement by Andy Deloney
Chairman
Michigan Liquor Control Commission

Chairman Franz,

I would like to thank you and the members of this committee for allowing me to have a statement read into the record. I apologize that I am not able to personally be present to make the statement myself, but I very much appreciate the ability to allow the Commission's professional staff to do so in my stead.

The Administration is **opposed** to the latest version of the bill, (H-2) Draft 5.

Revenue impact

In regard to the reduction in the mark-up, we estimate a negative impact on revenues of **\$6.5 million in the first year**.

In regard to the proposal that has been referred to as a "rebate", we estimate that these payments would negatively impact revenues by **\$4.9 million in the first year**.

Since receiving this latest draft on Friday evening, we have been performing precise calculations to get a more accurate projection of revenue impact, by looking at individual licensed small distillers and determining the kinds of payments they would receive under (H-2) Draft 5.

Currently, there are more than 70 licensed small distillers in Michigan, an additional 21 small distiller license applications pending consideration by the Commission, and a currently unknown number of out-of-state businesses who hold their state's substantial equivalent of a small distiller license, who would be entitled to payments under this proposal.

With a payment of \$15 per gallon sold, **eight** small distillers in Michigan that we reviewed would be entitled to **payments totaling \$806,082**. For these eight licensees, we looked at their total sales to the state for the 52 weeks of fiscal year 2016.

Also of note, we have not yet been able to determine the total amount of payments to which out-of-state small distillers would be entitled. Therefore, we do not have an estimate of the revenue impact from payments made to those distillers.

It should also be noted that the total number of qualifying small distillers, and the size of the checks the state will have to write, will increase as the number of small distillers grows, and as their sales grow.

Thoughts for consideration

Since (H-2) Draft 5 was distributed on Friday evening, I have been considering this payment concept further. I would ask this committee and the Legislature to consider the following points regarding this proposed payment system:

1. What is being proposed is a payment system to assist small distillers. The payment system language:
 - a. would create **annual payments of up to \$900,000** per small distiller in Michigan and out-of-state,
 - b. has **no sunset**,
 - c. has **no limit** on the number of times a licensed small distiller or their equivalents could receive this payment, and
 - d. ironically increases the size of the payments as the small distiller's sales increase.
2. According to our review, one Michigan licensed small distiller alone would be entitled to a payment of \$206,295 based on their sales in FY 2016. If this same distiller's sales increase in the next year, so would their payment from the taxpayers of the state. **The question I ask this committee and the Legislature is this:** Is it good public policy to create an unlimited, unending system of payments to provide assistance to distillers in this state, with some distillers to receive annual payments of hundreds of thousands of dollars, and where the amounts of the checks will increase annually as their companies grow?
3. This concept has been erroneously referred to as a "rebate". The Legislature should be aware, however, that what is proposed is not a rebate, but rather a system of payments to assist small distillers. And the more the small distiller sells to the state, the more the small distiller is entitled to in the form of an annual payment.

The liquor control code currently includes a true rebate system for licensed micro brewers. Under the statute, qualifying licensed micro brewers can receive a rebate on taxes paid to the state, up to \$2 per barrel. What is proposed here is nothing of the sort.

Under the proposed concept here, the small distiller sells their product to the state, is paid for the sale by the state, and yet will now be entitled to an additional payment annually from the state, on top of what was paid by the state for their products. In short, while the licensed micro brewer pays taxes and gets a small portion back, the small distiller makes a sale, gets paid for the sale, and then gets an additional payment at the end of the year for up to \$900,000.

So we paid them for their product, and now we will have to pay them *again*, because they sold us their product.
4. If the impetus for this payment concept is to assist small distillers, then shouldn't the value of the payments decrease as the small distillers become more successful? Under this proposal, the small distiller with the least in sales is entitled to the least in annual payments, in contrast to the largest of the small distillers, who would be entitled to the largest annual payments.
5. As of this writing, we have not even had a chance to determine how many out-of-state small distillers would be entitled to these payments, or how much in assistance the taxpayers would have to pay to them. Therefore, we cannot estimate what revenue loss would be attributed to out-of-state small distillers at this time.
6. Finally, (H-2) Draft 5 does not include language to address the issue of licensed small distillers under common ownership. The language appeared in previous drafts, yet was not included in this draft.

Estimated Annual Payment Total For Each Year 2018 thru 2036 and Beyond
Computed at \$15 per Gallon

<u>Licensees</u>	<u>FY 2015 - 16 Gallons</u>	<u>Payment at \$15 per Gallon</u>	<u>To Compute An Average</u>	<u>Payments</u>
Fish Hook	13,753.24	\$ 206,298.60		\$ 206,298.60
New Holland	12,968.56	\$ 194,528.40		\$ 194,528.40
TCWC, LLC	11,751.12	\$ 176,266.80		\$ 176,266.80
Two James	6,963.41	\$ 104,451.15	\$ 104,451.15	
Journeyman	4,167.34	\$ 62,510.10	\$ 62,510.10	
Grand Traverse	2,566.84	\$ 38,502.60	\$ 38,502.60	
Long Road	1,213.87	\$ 18,208.05	\$ 18,208.05	
Working Bugs	376.88	\$ 5,653.20	\$ 5,653.20	
	53,761.26	806,418.90	\$ 229,325.10	
Average Payment for Five Current No. of Licenses (77 Total)			\$ 45,865.02 74	
Subtotal *			<u>\$ 3,394,011.48</u>	\$ 3,394,011.48
Total Annual Payment (based on current licenses) *				<u><u>\$ 3,971,105.28</u></u>
Number of Pending Licenses			21	
Potential Payment for Pending Licenses *			<u><u>\$ 963,165.42</u></u>	
Grand Total Annual Payment *				<u><u>\$ 4,934,270.70</u></u>

* Amounts do not include any payments to out-of-state businesses determined to be substantially equivalent to a licensed small distiller.

Calculation explanation:

Eight licensed small distillers were selected and the gallons they sold to the state were calculated based on weekly purchase orders. An average payment was calculated to be applied to the remaining licenses. To calculate a reasonable average payment, the three (out of the eight selected) highest payment amounts were removed from the average calculation. The payment average was applied to the remaining 74 licenses and then the three highest actual payment amounts were added to the total for the 74. There are currently 21 pending small distiller license applications submitted to the commission.

Estimated Reduced Revenue Due To Mark Up Reductions
Each Year is Compared with FY 2015 Financial Results

<u>Year</u>	<u>Mark Up</u>		<u>GF/GP</u>	<u>School Aid</u>		<u>Conv. Fac.</u>	<u>Retail</u>
	<u>Percent</u>			<u>Fund</u>	<u>Dev. Fund</u>		<u>Licenses</u>
2018	64.0%	\$	5,922,849.68	\$ 195,115.32	\$ 195,115.32	\$	1,162,280.60
2019	63.5%	\$	9,170,167.03	\$ 344,417.27	\$ 344,417.27	\$	1,796,813.88
2020	63.0%	\$	12,417,484.38	\$ 493,719.21	\$ 493,719.21	\$	2,431,347.15
2021	62.5%	\$	15,664,801.73	\$ 643,021.16	\$ 643,021.16	\$	3,065,880.43
2022	62.0%	\$	18,912,119.08	\$ 792,323.11	\$ 792,323.11	\$	3,700,413.71
2023	61.5%	\$	22,159,436.43	\$ 941,625.05	\$ 941,625.05	\$	4,334,946.98
2024	61.0%	\$	25,406,753.78	\$ 1,090,927.00	\$ 1,090,927.00	\$	4,969,480.26
2025	60.5%	\$	28,654,071.14	\$ 1,240,228.95	\$ 1,240,228.95	\$	5,604,013.53
2026	60.0%	\$	31,901,388.49	\$ 1,389,530.90	\$ 1,389,530.90	\$	6,238,546.81
2027	59.5%	\$	35,148,705.84	\$ 1,538,832.84	\$ 1,538,832.84	\$	6,873,080.08
2028	59.0%	\$	38,396,023.19	\$ 1,688,134.79	\$ 1,688,134.79	\$	7,507,613.36
2029	58.5%	\$	41,643,340.54	\$ 1,837,436.74	\$ 1,837,436.74	\$	8,142,146.63
2030	58.0%	\$	44,890,657.89	\$ 1,986,738.68	\$ 1,986,738.68	\$	8,776,679.91
2031	57.5%	\$	48,137,975.25	\$ 2,136,040.63	\$ 2,136,040.63	\$	9,411,213.19
2032	57.0%	\$	51,385,292.60	\$ 2,285,342.58	\$ 2,285,342.58	\$	10,045,746.46
2033	56.5%	\$	54,632,609.95	\$ 2,434,644.53	\$ 2,434,644.53	\$	10,680,279.74
2034	56.0%	\$	57,879,927.30	\$ 2,583,946.47	\$ 2,583,946.47	\$	11,314,813.01
2035	55.5%	\$	61,127,244.65	\$ 2,733,248.42	\$ 2,733,248.42	\$	11,949,346.29
2036 *	55.0%	\$	64,374,562.00	\$ 2,882,550.37	\$ 2,882,550.37	\$	12,583,879.56
Total Revenue Lost		\$	667,825,410.95	\$ 29,237,824.02	\$ 29,237,824.02	\$	130,588,521.58

* The revenue amounts that will be lost during 2037 and all future years will be the same as the amounts that were lost during the 2036 year.